Internal Revenue Service

memorandum

CC:TL:-N-7882-90
TL/P/WHEARD/lmr

date: OCT 9 1990

to: District Counsel, Boston CC:BOS
Attn: Gary Gross

from: Assistant Chief Counsel (Tax Litigation) CC:TL

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subject: [redacted]
TL-N-7882-90
CC:TL:TS Heard Sabin
FDIC Bankruptcy as Event Converting Partnership Items; Effect of Receivership on Settlement Agreement; I.R.C. §§ 6231(c), 6231(b)(1)(C)

This memorandum responds to your request for Tax Litigation Advice.

ISSUES

1. Whether, in a non-judicial receivership proceeding in which the Office of Thrift Supervision (OTS) appoints the Federal Deposit Insurance Corporation (FDIC) as receiver of an insolvent bank under section 5(d)(2) of the Home Owner's Loan Act of 1933 (HOLA), the bank's partnership items are converted to non-partnership items pursuant to Temp. Treas. Reg. § 301.6231(c)-7T(b)?

2. Whether a settlement agreement executed prior to the receivership of the Bank by its Senior Vice President and Chief Financial Officer is valid?

CONCLUSIONS

1. The partnership items are not converted to nonpartnership items as of the date of the appointment of the FDIC as receiver.

2. The settlement agreement is valid. Furthermore, the settlement agreement converted the partnership items of the Bank to nonpartnership items as of the date of execution by the Service.

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FACTS

[redacted], (the bank) is a federally chartered savings association, the accounts of which are insured by the FDIC. The bank is a partner of [redacted], a partnership covered under TEFRA provisions.

On [redacted], OTS found and determined that the bank was in unsafe and unsound condition to transact business, due to having substantially insufficient capital and that, therefore, a ground for the appointment of a receiver for the bank existed under the HOLA. Furthermore, pursuant to the aforementioned section, as amended by section 301 of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA), OTS appointed the FDIC as sole receiver of the bank. On [redacted], the FDIC took possession of the bank and succeeded to all rights, titles, powers and privileges of the bank.

By letter dated [redacted], the FDIC notified the creditors of the bank that the bank was closed and that the FDIC was appointed receiver. The letter also instructed the creditors to file their claims with proof no later than [redacted], in order to have their claims considered by the receiver or their claim may be forfeited.

On [redacted], prior to the appointment of the FDIC receiver, the Bank executed Forms 870-L agreeing to adjustments for the fiscal years ending [redacted], [redacted] and [redacted]. However, the forms were not executed by the Service until [redacted], a date subsequent to the appointment of the receiver. Although the receiver was appointed on [redacted], the Service did not receive actual notice until February 7, 1990.

DISCUSSION

The first issue that you raise is whether pursuant to Temp. Treas. Reg. § 301.6231(c)-7T(b), the bank's partnership items were converted into nonpartnership items as of the date of the appointment of the FDIC as receiver. This temporary regulation was promulgated pursuant to I.R.C. § 6231(c) which allows the Service, in the case of an area that the Secretary determines to present special enforcement considerations, to promulgate regulations to treat items as nonpartnership items if treatment as partnership items will interfere with the effective and efficient enforcement of the internal revenue laws. The regulation states:

> (b) Receivership. The treatment of items as partnership items with respect to a partner for whom a receiver has been appointed in any receivership proceeding before any court of the United States, or of any State, or of the District of Columbia will interfere with the effective and efficient enforcement of the internal revenue laws.
>
> Accordingly, partnership items of such partner arising in any partnership taxable year ending on or before the last day of the latest taxable year of the partner with respect to which the United States could file a claim for income tax due in the receivership proceeding shall be treated as non-partnership items as of the date a receiver is appointed in any receivership proceeding before any court of the United States or of any State or the District of Columbia.

Temp. Treas. Reg. § 301.6231(c)-7T(b)

In this case, the FDIC's appointment as receiver of the bank is a statutory as opposed to a court-ordered receivership. See 12 U.S.C. § 191, 1821(c); In the Matter of the Liquidation of American City Bank and Trust Company, 402 F.Supp. 1229, 1231 (E.D. Wis. 1975). The receiverships of national banks are a unique system created by Congress under the money and currency clause of the Constitution. Id. The FDIC, as a receiver of a national bank differs from an ordinary receiver in that the FDIC is not an officer of a court but is an officer of the executive branch of government and the bank's assets are not in the custody of a court. 80 Pine Inc. v. European and American Bank, 424 F.Supp. 908 (E.D.N.Y. 1976); Wittnebel v. Loughman, 9 F.Supp. 465, 467 (S.D.N.Y. 1935). Therefore, in the case of an FDIC receivership, there is no receivership proceeding pending before a court of the United States, any state, or the District of Columbia. Therefore, Temp. Treas. Reg. § 301.6231(c)-7T(b) does not operate to convert the bank's partnership items to non-partnership items as of the date of the appointment of the FDIC as receiver. This conclusion is consistent with the purpose underlying the apparent regulatory purpose of section 301.6231(c)-7T(b).

The primary reason for having items convert under this regulation is that, in a judicial bankruptcy proceeding, all civil proceedings with respect to the debtor are stayed pursuant to 26 USC 362. A TEFRA proceeding is a civil proceeding with

respect to all partners in the partnership. Thus, if even one partner out of a hundred is a debtor in a judicial proceeding, the TEFRA proceeding would be stayed. The above regulation was needed to remove the debtor partner from the TEFRA proceeding. Since the debtor partner would no longer be subject to the TEFRA proceeding, the above stay provision would no longer prevent the continuance of the proceeding with respect to the non-debtor partners. Cf. Computer Programs Lambda, Ltd. v. Commissioner, 89 T.C. 198 (1987).

No stay provision exists with respect to HOLA receiverships. Thus, the fact that the naming of a receiver does not convert the Bank's partnership items does not interfere with the progress of the TEFRA proceeding.

Validity of Form 870-L

As noted above, the Bank executed a Form 870-L (through its Senior Vice President and Chief Financial Officer). If valid, this constitutes a settlement agreement pursuant to I.R.C. § 6224(c) agreeing to the assessment and collection of a deficiency in tax. Furthermore, such a settlement agreement converts the agreed to items to nonpartnership items pursuant to section 6231(b)(1)(C). Conversion of partnership items results in the Bank no longer being a party to the ongoing TEFRA proceeding. I.R.C. § 6226(c) and (d). Agreed to items may be directly assessed. I.R.C. § 6230(a)(2)(A)(ii).

If the agreement is valid, the claim for the assessed amount may be submitted directly to the receiver. The claim would not have to await the outcome of the TEFRA proceeding. If the claims have to await the outcome of the TEFRA proceeding it is likely that the receiver will have disposed of all assets.

In any event, this issue now appears to be moot. Attached to your incoming memorandum is a memorandum dated May 11, 1990 from the examination division. This memorandum indicates that the losses from other sources are so great no tax is generated by the closing agreement even if it is valid.

Nevertheless, we are coordinating this issue with the General Litigation Division and Financial Institutions and Products for your future use. Pending receipt of their responses, however, our conclusions are as follows:

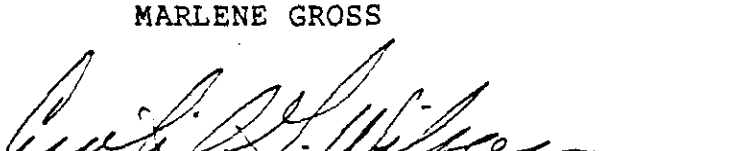
Initially we note that there is no provision under HOLA which makes previously executed determinations of liabilities void or voidable, unlike the judicial bankruptcy provisions. It appears that the receiver appointed by the FDIC merely "succeeds" to the powers of the existing bank agents. 12 USC § 1821(I). Nonetheless, the receiver may limit the amount payable under an agreement under general principles of receivership.

Because there is no direct statutory provision under HOLA governing the validity of such agreements, common law should control. At the time the Bank executed the agreement, the agent who signed had authority to do so. On the date a receiver was appointed, he lost his status as an agent. The termination of an agent's authority does not thereby terminate his apparent authority until the third person has notice of the termination. Restatement of Agency 2nd, § 125. Thus, the Bank's offer remained outstanding until the government/offeree learned of the termination of the agent's status. Since the offer was accepted prior to receipt of notification, we conclude that the settlement agreement was validly executed. Thus, our position is that it converted the agreed to items to nonpartnership items pursuant to section 6231(b)(1)(C).

We will inform you if the responses we receive from other divisions result in a different answer.

Please refer any questions on this matter to Bill Heard at FTS 566-3289.

MARLENE GROSS

By: 

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